

GAO

Testimony

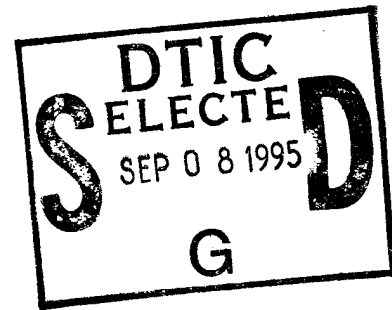
Before the Subcommittee on Oversight and Investigations,
Committee on Energy and Commerce,
House of Representatives

For Release
on Delivery
Expected at
10:00 a.m. EDT
Wednesday
July 8, 1992

SUPERFUND

Actions Needed to Correct
Long-Standing Contract
Management Problems

Statement of
J. Dexter Peach, Assistant Comptroller General
Resources, Community, and Economic Development Division



19950905 098

DISTRIBUTION STATEMENT A
Approved for public release;
Distribution Unlimited

Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to be here today to discuss the Environmental Protection Agency's (EPA) efforts to correct long-standing contract management problems in the Superfund program. Superfund, EPA's \$15 billion effort to clean up the nation's most dangerous hazardous waste sites, is 1 of 16 federal programs that GAO has identified as being most vulnerable to fraud, waste, and abuse. The program is vulnerable in part because of its extensive use of cost-reimbursable contracts, with potential values of almost \$10 billion, and its history of contract management problems.

Our testimony today is based on our involvement, since 1988, in Superfund contract management-related issues and especially our October 1991 report on Superfund contracting.¹ (Appendix I lists our relevant reports and testimonies.) Our reports have addressed a variety of significant contract management problems, including some this Subcommittee has already dealt with extensively, such as inadequate contract audit coverage and excessive contractor program management costs. Today I would like to highlight our findings on three other contract management problems: contractor cost controls, indemnification, and conflict of interest. I would also like to discuss the root causes of these problems, the reasons for their persistence and recent EPA plans to make improvements.

In summary, last October we reported that EPA had not fully addressed numerous GAO recommendations to reduce the Superfund program's vulnerability to fraud, waste, and abuse--despite several years of our reporting on these deficiencies. Specifically, we reported that controls over contractor costs, such as critical reviews of contractor cost proposals and invoices, were often not being used. In addition, Superfund's exposure to indemnification losses was unlimited because regulations to limit coverage had yet to be issued. Moreover, Superfund remained vulnerable to contractors' conflicts of interest because EPA contracting officials still needed better guidance on what constitutes a conflict, and field checks of contractors' compliance with conflict-of-interest rules had not yet been performed.

We reported that EPA management had made some effort in the past to correct these problems but had failed to follow through on its planned improvements. The persistence of problems was largely the result of EPA's lack of sustained high-level attention to Superfund contract management and its delegation of contract management authority to the regions without sufficient accountability and oversight. Our report made several recommendations to improve the specific problems and to deal with the underlying causes.

¹Superfund: EPA Has Not Corrected Long-Standing Contract Management Problems (GAO/RCED-92-45, Oct. 24, 1991).

In the past year, public disclosure through congressional oversight and press reports of high and, in some cases, unallowable contractor charges forced EPA to take a fresh look at how it was managing its Superfund remedial contracts. Consistent with many of our prior recommendations, the agency made organizational and procedural changes and set up some internal oversight groups to strengthen accountability for contract management. We think that these efforts have merit, but they are only a beginning. To make permanent improvements, EPA will have to carry through on its initiatives--something it has repeatedly failed to do in the past.

Before discussing each of these issues in more detail, I would like to briefly review, for the Subcommittee, the Superfund program's history and operation and some of GAO's earlier reports that initially identified problems with cost control, indemnification, and conflict of interest.

BACKGROUND

The Superfund program was created by the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 to clean up the nation's most dangerous hazardous waste sites. The program has been reauthorized twice since then--first, in 1986, by the Superfund Amendments and Reauthorization Act (SARA) and again in 1990. The program's cumulative authorization is \$15.2 billion.

The scope and cost of Superfund have greatly exceeded initial expectations. The Superfund cleanup list, which originally included 406 sites, currently contains 1,275 sites, and EPA expects the list to grow to 2,000 sites by the year 2000. While the program has had some important accomplishments, especially in alleviating emergency conditions at sites and enforcing cleanup obligations of those who contaminated the sites, cleanups have been completed at only 90 sites. Consequently, we can expect the cleanup effort at present Superfund sites alone will run well into the next century. Superfund's authorization through 1994 will not come close to paying for EPA's projected \$40 billion share of cleanup costs for the currently listed sites. In this context, efficient use of Superfund resources, including contracting resources, is critical to the program's ultimate success.

As the Subcommittee is well aware, EPA relies heavily on private contractors to help carry out Superfund cleanups. About 40 percent of the program's funds have been obligated for contractors, mostly through cost-reimbursable contracts. These contracts are authorized by federal regulations and are appropriate in some circumstances. But compared with fixed-price contracts, they transfer more of the risk of unexpected cost increases to the government. The largest group of cost-reimbursable Superfund contracts consists of 44 contracts, collectively valued at more than \$6 billion. These 10-year contracts were awarded to 23 prime contractors to conduct cleanup studies, design remedies, and

oversee construction at sites. EPA has largely delegated the administration of these contracts to its regional offices.

Cost-reimbursable contracts require effective EPA oversight to protect against abuses. In 1988 we reported that EPA was neglecting some very basic contract management techniques. Specifically, EPA was not adequately reviewing (1) contractor cost proposals for cleanup studies, which are the basis of budgets developed for these studies, and (2) contractor invoices--bills the contractor submits monthly as work at sites progresses. Because EPA was not estimating what cleanup studies should cost, it had to rely too much on contractor estimates. Moreover, EPA officials who negotiated budgets with contractors for cleanup studies were not documenting the negotiation process, even though such records force officials to justify their price agreements and can be very valuable in future negotiations.

In 1989 we reported that EPA had indemnified contractors too liberally, putting Superfund assets at excessive risk. The Superfund law authorized EPA to indemnify contractors, that is, to pay for any damages that their negligent work at Superfund sites caused. This indemnification was to be granted only up to a limit to be specified by EPA and only to contractors who could not obtain private insurance at a reasonable cost. We found, however, that EPA had not established an indemnification limit nor required contractors to apply for insurance before being indemnified.

In 1989 we also reported that Superfund was vulnerable to contractor conflicts of interest because the same contractors who helped EPA to choose cleanup remedies also could work for the parties responsible for paying for the remedies. Yet, we found that EPA had not taken several important steps to safeguard against potential conflicts of interest. For example, EPA did not clearly instruct contractors and EPA personnel on what activities constituted conflicts nor check contractors' compliance with its conflict-of-interest rules.

In response to requests from this and other congressional committees, we followed up on these reports to see if EPA had corrected the problems they disclosed. Our October 1991 report showed that little had been done. Let me now focus on the findings of this report in each of the areas I highlighted earlier: cost control, indemnification, conflicts of interest, and the root causes of contract management neglect.

Accession For	
NTIS	<input checked="checked" type="checkbox"/>
CRA&I	<input type="checkbox"/>
DTIC	<input type="checkbox"/>
TAB	<input type="checkbox"/>
Unannounced	<input type="checkbox"/>
Justification	
By	
Distribution /	
Availability Codes	
Dist	Avail and/or Special
A-1	

BETTER CONTROLS NEEDED OVER CONTRACTOR COSTS

First, with regard to cost control, we found continued failure on the part of EPA to examine contractor budgets and bills and to document price negotiations. EPA still was not requiring its regional offices to prepare cost estimates of cleanup studies, which were budgeted for \$342 million in fiscal years 1988 through 1990. As a result, the regions were still too dependent on the contractors' own cost proposals. The four EPA regions GAO visited --Regions I, II, III, and V--had prepared cost estimates independent from the contractors', for only 4 of 30 sampled cleanup studies. When prepared, they were used to reduce the contractor's proposal--in one case from \$3 million to \$1.6 million.

In the absence of adequate cost control, contractors' studies have been getting more expensive. An EPA consultant found that the doubling of these studies' costs that occurred between 1985 and 1988 was, in part, caused by a lack of adequate cost control.

Although EPA did require Superfund project managers to review contractor invoices for reasonableness, compliance continued to be inconsistent. Contracting officials in two of the four regions estimated that project managers were conducting invoice reviews for only about half of their contractors' invoices.

In the absence of effective contractor oversight by both headquarters and field personnel, Superfund money can be wasted. For example, as you know, we testified before this Subcommittee in March 1992 that CH₂M Hill, a consulting engineering firm and one of Superfund's largest contractors, included expenses in its indirect cost pool (a portion of which is charged to EPA) that were not allowable under the Federal Acquisition Regulations (FAR).² In examining selected indirect cost accounts, such as meals, lodging, and relocation expenses, we identified about \$2.3 million in indirect costs that the FAR does not allow. These expenses included tickets to professional sporting events, alcohol at company parties, and travel by nonemployee spouses. In addition to the unallowable costs, we identified indirect costs of \$266,500 that, while not specifically unallowable, appeared questionable for allocation to federally sponsored contracts. CH₂M Hill has responded that the unallowable and questionable costs are offset by a discount in prices that the contractor provides to the government. Although we are not opposed to contractors offering the federal government a real discount, contractors must remove unallowables and account for its costs in accordance with the FAR regardless of whether it subsequently chooses to offer a discount.

²Federally Sponsored Contracts: Unallowable and Questionable Indirect Costs Claimed By CH₂M Hill (GAO/T-RCED-92-37, Mar. 19, 1992).

In addition, we found that price negotiation records were still not being prepared for contractors' projects. None of the files we reviewed for 30 remedial studies contained documentation equivalent to what is required by the FAR for contract negotiations. The absence of adequate negotiations records will make it difficult for EPA to judge whether improvements are in fact being made in its price negotiations with contractors.

CONTRACTOR INDEMNIFICATION STILL TOO LIBERAL

The second issue that I would like to discuss is continuing excessive contractor indemnification, which we first reported almost 3 years ago. This problem has the potential to seriously drain Superfund resources.

Our 1991 report discussed three persistent contract indemnification concerns. First, EPA had not adequately determined contractors' needs for indemnification--that is, the minimum indemnification necessary to ensure an adequate supply of contractor services, even though considerable evidence showed that contractors would be willing to participate in Superfund at lower indemnification levels than were granted. Furthermore, EPA had not established a ceiling on indemnification per contract as required by the 1986 Superfund reauthorization act. In the absence of the ceiling, each indemnification agreement is currently backed by the entire unobligated balance of Superfund. Second, EPA had not ensured that indemnification was provided only after contractors proved their inability to purchase private insurance, another SARA requirement. Third, other federal agencies were indemnifying their Superfund contractors under general procurement regulations even though SARA establishes more restrictive provisions for indemnifying Superfund contractors. EPA had not notified other federal agencies, as we recommended, of the need to use SARA's indemnification provisions.

The longer EPA delays in setting a limit on indemnification agreements, the longer Superfund remains exposed to liability not intended by SARA. As of September 1991, about 30 cleanup contracts with unlimited indemnification have expired. With their expiration, EPA has lost the opportunity to limit its liability risk on these contracts.

CONTRACTOR CONFLICTS OF INTERESTS CAN MAKE SUPERFUND VULNERABLE

I would like to turn now to a third issue--the continuing vulnerability of Superfund to conflicts of interest. Potential contractor conflicts of interest can arise in the Superfund program because many of the contractors that help EPA select and implement cleanup remedies also can work for the parties responsible for paying for cleanups. Contractors' work for these parties could impair contractors' objectivity when performing work for EPA.

Also, contractors could have access to sensitive EPA enforcement information advantageous to these same parties.

Since 1989 we have reported continuing problems in EPA's organizational conflict-of-interest system, including inadequate guidance and insufficient verification of compliance with conflict-of-interest rules. For example, because potential conflicts of interest are often not clear-cut, contracting officers need guidance to identify and resolve conflicts consistently. But, some contracting officers complained that current conflict-of-interest guidance was of little or no help. They said that additional guidance and examples of what constitutes a conflict of interest would be helpful in evaluating and resolving conflicts.

Moreover, since EPA's conflict-of-interest control system relies heavily on self-disclosure, this system can only be credible if EPA maintains sufficient oversight of contractors. We reported that EPA had not done independent checks to verify contractors' compliance with conflict-of-interest policies. For example, as of June 1992, only 4 out of about 80 Superfund contractors' systems have been reviewed and only one more review is planned in fiscal year 1992.

HIGH-LEVEL ATTENTION TO ROOT CAUSES NEEDED

I would now like to discuss the root causes of EPA's chronic Superfund contract management problems. EPA has acknowledged many of the problems we have reported in the past, but until recently, it had not addressed our recommendations. A pattern is apparent in EPA's response to reported contract management deficiencies: extended study of the problems, sometimes leading to revised plans or procedures, but with insufficient follow-through to actually correct the problems.

The persistence of these problems is largely the result of EPA's lack of sustained attention to Superfund contract management. As far back as 1988, we reported that EPA management's primary focus has been on the speed and the quality of cleanups and the enforcement of responsible party obligations. This priority was reflected in the attitudes of EPA project managers we interviewed, who generally rated quality and timeliness over cost as considerations in managing their projects. Although these are certainly important objectives, they should not be achieved at the expense of sound contract management practices. As we stated in our 1991 report, we believe that top agency managers must intervene, raise the level of concern throughout the agency with contractor cost control and other contracting issues, and see these issues through to resolution. In short, since contracting is crucial to the success of the Superfund program, EPA's culture needs to be changed to put greater emphasis on sound contract management.

A second underlying cause of the failure to correct the deficiencies discussed in our previous reports has been EPA headquarters' delegation of management responsibility to the regions without sufficient oversight and accountability. Our 1991 report showed that the regions had not received enough advice or training from headquarters on estimating contractor costs, reviewing claimed costs, and dealing with contractors' potential conflicts of interest. Nor had the regions fully adhered to headquarters' policy on invoice review, indemnification, and conflict-of-interest controls. While a decentralized approach to contract administration can be effective, it must be accompanied by headquarters' assistance when regions need it; accountability in the regions for performance; and enough oversight to ensure that national priorities, such as cost control, are observed.

RECENT EPA ACTIONS

After years of inattention, EPA under outside pressure acknowledged last fall that it has a serious Superfund contract management problem and has finally begun to take corrective action. After the issuance in October 1991 of our report and an EPA Superfund contracting task force report that confirmed our findings, EPA concluded that it was not conducting effective Superfund contract administration and oversight and initiated a number of contract reforms.

First, as we recommended to better control costs, EPA has recently required regions to develop independent government cost estimates for Superfund cleanup studies performed by contractors. The agency also instructed regions to more thoroughly review contractor invoices and took other actions consistent with the recommendations made by our reports.

Second, to ensure greater management attention and accountability, EPA reported Superfund contract management as a material weakness in its December 1991 Federal Managers' Financial Integrity Act report. This action was also in conformance with our recommendation. In addition, in late February 1992, the agency elevated the procurement function within the organization and made senior EPA officials accountable for procurement in each major office. Moreover, in March of this year, EPA established a Standing Committee on Contracts Management to conduct a thorough review of procurement and contract management in EPA. The primary objective of this committee is to identify major systemic contract management problems and to recommend corrective actions. As you know, EPA plans to discuss the committee's report at today's hearing.

Since our latest report, however, there has been limited progress on the remaining two issues we discussed--strengthening controls over contractor indemnification and conflicts of interest. EPA has prepared new indemnification guidelines and conflict-of-

interest rules, but neither has been approved yet by the Office of Management and Budget. Moreover, EPA has provided little additional conflict-of-interest guidance to regional staff and has checked the compliance of only one additional contractor with the conflict-of-interest requirements because of resource limitations.

CONCLUSIONS

In conclusion, EPA's extensive use of cost-reimbursable contracts in the Superfund program imposes on it a special responsibility for effective cost control. To date, EPA has not lived up to this responsibility. Until recently, despite repeated warnings of contract management problems, EPA top management attention has not been focused on this area.

EPA's promises to improve contracting activities are a hopeful start to correcting these long-standing contracting problems. However, it is crucial for EPA to follow through on these promises --an area in which EPA has fallen short in the past. Unless the effort is sustained and substantive changes occur, scarce Superfund resources will remain highly vulnerable to fraud, waste, and abuse.

- - - - -
Mr. Chairman, this completes my prepared statement. I will be glad to respond to any questions that you or Members of the Subcommittee may have.

RELATED GAO PRODUCTS

Federally Sponsored Contracts: Unallowable and Questionable Indirect Costs Claimed by CH₂M Hill (GAO/T-RCED-92-37, Mar. 19, 1992).

Superfund: Issues That Need To Be Addressed Before the Program's Next Reauthorization (GAO/T-RCED-92-15, Oct. 29, 1991).

Superfund: EPA Has Not Corrected Long-Standing Contract Management Problems (GAO/RCED-92-45, Oct. 24, 1991).

EPA's Contract Management: Audit Backlogs and Audit Follow-up Problems Undermine EPA's Contract Management (GAO/T-RCED-91-5, Dec. 11, 1990).

Superfund: Contractors Are Being Too Liberally Indemnified by the Government (GAO/RCED-89-160, Sept. 26, 1989).

Making Superfund Work Better: A Challenge for the New Administration (GAO/T-RCED-89-48, June 15, 1989).

Superfund Contracts: EPA's Procedures for Preventing Conflicts of Interest Need Strengthening (GAO/RCED-89-57, Feb. 17, 1989).

Sound Contract Management Needed at the Environmental Protection Agency (GAO/T-RCED-89-8, Feb. 23, 1989).

Superfund Contracts: EPA Needs to Control Contractor Costs (GAO/RCED-88-182, July 29, 1988).